

395,2548 (9pgs)

2/8/94

STATE OF CALIFORNIA

BOARD OF EQUALIZATION

BUSINESS TAXES APPEALS REVIEW SECTION

In the Matter of the Petition  
for Redetermination Under the  
Sales and Use Tax Law of:

DECISION AND RECOMMENDATION

No. [REDACTED]

Petitioner

The Appeals conference in the above-referenced matter was held by Staff Counsel Sharon Jarvis on August 3, 1993 in Arcadia, California.

Appearing for Petitioner:

Petitioner submitted a written statement in lieu of appearing at an Appeals conference.

Appearing for the  
Sales and Use Tax Department:

Mr. Willard L. Smith  
Supervising Tax Auditor

Protested Item

The protested tax liability for the period October 1, 1987 through December 31, 1990 is measured by:

Item

State, Local  
and County

B. Capital asset sales not reported.

\$ 33,604

Petitioner's Contentions

There was no sale of assets for consideration. Rather, there was simply a bookkeeping adjustment to correct previous accounting misclassifications between a parent and a subsidiary company.

Summary of Petition

Petitioner, [REDACTED], is an optical laboratory. This is petitioner's first audit.

In 1987 petitioner became a wholly owned subsidiary of [REDACTED]. On October 1, 1989 [REDACTED] the general manager of petitioner, purchased all of the outstanding stock of petitioner from [REDACTED] for \$25,000. (Stock Purchase Agreement, attached as Exhibit A.) On the same day, according to two "Bill[s] of Sale", petitioner sold to [REDACTED] (1) optical surfacing equipment for a stated "cash price" of \$20,064, and (2) [REDACTED] system software for a stated "cash price" of \$13,000. (Bills of sale, attached as Exhibit B.) The "payment terms" were stated as "offset against stock purchase obligation dated October 1, 1989 between the parties". The bills of sale were signed by [REDACTED] as president of petitioner, and [REDACTED] as chairman of [REDACTED].

Petitioner contends that the assets were never sold and that there was no sale for consideration. Petitioner contends the assets were just transferred on the books of the parent and subsidiary companies. Petitioner states that when [REDACTED] acquired petitioner in 1987, the operations of the two companies were similar and commingled. Equipment and employees were shared by both companies without distinction, and cash and payroll centralized in [REDACTED]. Petitioner states that the only identity for petitioner was in the billing to customers; and that the two companies were different entities only in legal form. Petitioner further states:

"In 1989 [REDACTED] [petitioner] was sold to a [REDACTED] employee through the sale of the [REDACTED] stock. The companies remained collocated in the same building after the sale. In preparation for the sale an equipment inventory was taken and the assets acquired for the [REDACTED] operation identified. The assets acquired subsequent to the formation of [REDACTED] were accounted for in [REDACTED] property accounting regardless of which company had purchased the equipment. To account for the sale it was necessary to transfer the [REDACTED] assets on [REDACTED] accounting records to an [REDACTED] account in the consolidated general

[REDACTED]

ledger. This was done by journal entry and was documented by an equipment list erroneously entitled bill of sale. This is what your auditor picked up on and determined that a sale had taken place. There in fact was no sale, simply a bookkeeping adjustment to correct previous accounting misclassifications. The transfer did not involve any consideration between the companies.

"The only confusion is that the schedule of assets transferred were labeled 'bill of sale' to make it clear to the parties in the divestiture of the subsidiary that the assets were properly allocated to the right companies." (8/15/93 letter.)

In earlier correspondence, petitioner also cited the Macrodyne case (Macrodyne Industries, Inc. v. State Bd. of Equalization (1987) 192 Cal.App.3d 579) and stated that as there was no consideration in the instant case, there was no sale and, therefore, no taxable transaction. (8/6/91 letter.)

The Sales and Use Tax Department (Department) contends that although petitioner was a wholly owned subsidiary of [REDACTED], each of the companies were separate entities with separate ID numbers and articles of incorporation. The Department asserts that the transaction in question was a taxable sale from one entity to another.

#### Analysis and Conclusions

Under the Sales and Use Tax Law, sales tax is imposed for the privilege of selling tangible personal property at retail. (Revenue and Taxation Code section<sup>1</sup> 6051.) A sale includes, "[a]ny transfer of title or possession, exchange, or barter, conditional or otherwise, in any manner or by any means whatsoever, of tangible personal property for a consideration." (Section 6006(a); see also Sales and Use Tax Regulation 1595.) Consideration is a benefit conferred upon the promisor by another to which the promisor is not lawfully entitled, or any prejudice suffered by the other which is not imposed by law. (Civil Code section 1605.)

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<sup>1</sup>Unless otherwise indicated, all further references to code sections are to the Revenue and Taxation Code.

The two corporations, [REDACTED] and [REDACTED], were two distinct legal entities. Like many corporate entities in the business world, one was wholly owned by the other and they shared employees and equipment. [REDACTED], which owned [REDACTED], handled the cash and the payroll; [REDACTED] was used as a billing entity. None of this changes the fact that [REDACTED] was a separate entity when purchased by [REDACTED], and was sold as a separate business entity to [REDACTED].

A review of the Stock Purchase Agreement between [REDACTED] and [REDACTED], and of the two bills of sale for the assets in question, is conclusive on the issue of whether there was a taxable sale. Our review reveals that the Stock Purchase Agreement was consummated first; and that afterwards petitioner, which was no longer a subsidiary of [REDACTED], sold the assets in question to [REDACTED]. This sequence of the events is clear because the bills of sale are signed by [REDACTED] as president of [REDACTED], the company whose stock he had just purchased. Prior to the stock purchase, [REDACTED] was not the president of petitioner and could not have legally signed the bills of sale as such.

The bills of sale for the assets transferred are evidence of a transfer of assets for consideration between two separate entities, a taxable transaction. This was not a transaction between a parent and a subsidiary, and it was not simply a bookkeeping adjustment. Despite petitioner's protests to the contrary, there was consideration for this sale: the offset of the cash price against the stock purchase obligation for [REDACTED] to purchase [REDACTED].

Moreover, even if these transactions had been transfers between a parent corporation and its wholly owned subsidiary corporation, characterized as transfers of equipment, the transactions still would be taxable sales for sales tax purposes where, as here, there were transfers of titles for consideration. (See Mercedes-Benz v. State Bd. of Equalization (1982) 127 Cal.App.3d 871.)

As to petitioner's earlier reference to the Macrodyne case, since this argument was not raised in the written statement submitted by petitioner in lieu of appearing at the Appeals conference, it appears that petitioner has abandoned this approach. We note, however, that while in Macrodyne the Court of Appeal found that there was no consideration in certain cases involving assumptions of liabilities, in the recent case of Beatrice Company v. State Board of Equalization (1993) 6 Cal.4th 767, the California Supreme Court disapproved the Macrodyne holding that there was no consideration when a transferor remained jointly liable with a transferee which has assumed a liability.

Recommendation

It is recommended that the Petition for Redetermination be denied; and that the determination be redetermined without adjustment.

Sharon Jarvis  
Sharon Jarvis, Staff Counsel

2-8-94  
Date

Attached: Exhibits A & B.

JA

## STOCK PURCHASE AGREEMENT

This Agreement made and entered into as of October 1, 1989 by and between \_\_\_\_\_ ("buyer") and \_\_\_\_\_ a California corporation ("seller").

### RECITALS

A. Seller owns all of the outstanding stock of \_\_\_\_\_ and operates such company as a subsidiary. Said issued stock represents 1,000 shares of the authorized shares of \_\_\_\_\_.

B. Buyer desires to purchase \_\_\_\_\_ as an operating company and to assume all of its assets and liabilities, customers and vendor relationships by purchasing the outstanding stock of \_\_\_\_\_ held by seller.

### AGREEMENT

1. Sale of Stock. Seller hereby agrees to sell and deliver to Buyer, and Buyer hereby agrees to buy, the Stock upon the terms and conditions set forth below.

2. Consideration. The Consideration for the Stock which Buyer shall pay to Seller at the Closing shall be \$25,000 in cash or a promissory note with terms agreed upon as embodied in the note attached hereto as exhibit A.

3. Sellers Representations and Warranties. Seller represents and warrants the following:

(a) That the \_\_\_\_\_ Balance Sheet attached hereto as Exhibit B and by this reference are a true and accurate statement of the financial position of \_\_\_\_\_ as of September 30, 1989.

(b) That \_\_\_\_\_ is a corporation in good standing with the State of California and its ancillary taxing authorities.

4. Buyers Representation and Warranties. Buyer represents and warrants the following:

(a) Buyer has a pre-existing personal or business relationship with Seller and in fact has operated the subject \_\_\_\_\_ subsidiary as general manager. By reason of such familiarity, and by reason of Buyer's own business and financial experience, Buyer has the capacity and knowledge to protect Buyer's interest in connection with this transaction.

5. Binding Agreement. All rights under this Agreement shall bind and inure to the benefit of the heirs, successors, personal representatives and assigns of each of the parties hereto, whether through merger, consolidation or otherwise.

EXHIBIT A

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6. Governing Law. This Agreement is entered into and to be performed in Los Angeles, California. This Agreement shall be construed and enforced in accordance with the laws of the State of California.

7. Attorney's Fees. In the event of any controversy, claim or dispute between the parties hereto, arising out of or relating to this Agreement or the breach thereof, the prevailing party shall be entitled to recover his reasonable attorney's fees incurred therein.

8. Entire Agreement. This Agreement contains the entire agreement of the parties relating to the right granted and obligations assumed in this Agreement. Any other agreements, representations, or modifications concerning this Agreement shall be of no force and effect unless contained in a writing signed by the parties to this Agreement.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed and delivered as of the date first written above.

"SELLER"

By

"BUYER"

BILL OF SALE

This Agreement is entered into this 1st day of October, 1989 by and between \_\_\_\_\_ (SELLER) and \_\_\_\_\_ (BUYER) both California corporations.

Seller agrees to sell and Buyer agrees to buy, subject to the terms and conditions herein, the following described personal property:

PROPERTY: OPTICAL SURFACING EQUIPMENT (Exhibit A)  
CASH PRICE: \$20,064.00  
PAYMENT TERMS: OFFSET AGAINST STOCK PURCHASE AGREEMENT  
DATED OCTOBER 1, 1989 BETWEEN THE PARTIES

Buyer hereby acknowledged receipt and possession of the subject personal property.

Seller consents and agrees to warrant and defend title of subject property against any person.

IN WITNESS, the parties execute this Agreement effective as of the date first written above:

By \_\_\_\_\_

President

By \_\_\_\_\_

Chairman

EXHIBIT

B

Page 1 of 2



# BILL OF SALE

This Agreement is entered into this 1st day of October, 1989 by and between [REDACTED] (SELLER) and [REDACTED] (BUYER) both California corporations.

Seller agrees to sell and Buyer agrees to buy, subject to the terms and conditions herein, the following described personal property:

PROPERTY: OMICS SYSTEM SOFTWARE (Exhibit A)  
CASH PRICE: \$13,000.00  
PAYMENT TERMS: OFFSET AGAINST STOCK PURCHASE OBLIGATION  
DATED OCTOBER 1, 1989 BETWEEN THE PARTIES

Buyer hereby acknowledged receipt and possession of the subject personal property.

Seller consents and agrees to warrant and defend title of subject property against any person.

IN WITNESS, the parties execute this Agreement effective as of the date first written above:

President

EXHIBIT

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